

**TESTIMONY OF AMERICAN BEVERAGE ASSOCIATION TO THE U.S.
DEPARTMENT OF AGRICULTURE, AGRICULTURAL MARKETING
SERVICE, WITH RESPECT TO PROPOSALS TO REVISE FLUID MILK
PRODUCT DEFINITION**

I am Drew Davis, Vice President of Federal Affairs for the American Beverage Association, American Beverage Association (ABA). The American Beverage Association has been the trade association for America's non-alcoholic refreshment beverage industry for more than 85 years. Founded in 1919 as the American Bottlers of Carbonated Beverages and renamed the National Soft Drink Association in 1966, ABA today represents hundreds of beverage producers, distributors, franchise companies and support industries. ABA's members employ more than 211,000 people who produce U.S. sales in excess of \$88 billion per year.

According to American Economics Group, Inc., direct, indirect and induced employment in the beverage industry means 3.02 million jobs that create \$278 billion in economic activity. At the state and federal level, beverage industry firms pay more than \$30 billion of business income taxes, personal income taxes, and other taxes with over \$14 billion in taxes paid to state governments alone. In 2003 it is estimated that beverage companies donated \$326 million to charities.

With innovation and creativity, our member companies have been developing a wide range of new products to maintain and expand consumer choices. Our members market literally hundreds of brands, flavors and packages, including carbonated soft drinks, ready-to-drink teas and coffees, bottled waters, fruit juices, fruit drinks, and sports drinks.

In addition, a number of our members have developed new products that utilize milk, or components thereof, as an ingredient. These new beverage products are generally classified as Class II because they contain less than 6.5 percent nonfat milk solids.

In response to the initial Dairy Farmers of America (DFA) request that the Agricultural Marketing Service (AMS) initiate a hearing to modify the fluid milk product definition, the American Beverage Association submitted a comment

urging that AMS not proceed to a hearing. We did not believe that there was any basis to suggest that the current definition is failing to properly classify products. Rather than forcing parties to proceed to the time and cost of a hearing, we argued that AMS should conduct an economic analysis to examine if these new products were in fact competing with fluid milk for consumers.

Unfortunately, AMS has ignored our request and proceeded to this public hearing, without conducting any economic analysis and despite the fact there is no demonstrable evidence that the current system is not working. Nevertheless, I am pleased to be here today to reiterate the American Beverage Association's position with respect to proposals to amend the fluid milk product definition.

The Fluid Milk Product Definition Covers Products That Compete With Or Substitute for Fluid Milk.

In general, AMS is required to classify products according to their form and use. In particular, the fluid milk product definition is intended to cover products that compete with or substitute for fluid milk. Fluid milk is a higher value product than other dairy products. By treating dairy products that compete with fluid milk for consumer dollars as Class I, the fluid milk product definition, in theory, helps to ensure that producers receive more of a benefit from these products than they would receive if the products were Class II (or some other classification).

The fundamental framework of the current classification system was established in 1974. 39 Fed. Reg. 9012 (March 7, 1974). In that 1974 decision, AMS excluded products that contain less than 6.5 percent nonfat milk solids from the fluid milk definition because they do not compete with fluid milk. Quote, "fluid products containing only a minimal amount of nonfat milk solids are not considered as being in the competitive sphere of the traditional milk beverages." Id. at 9015. The decision goes on to state that the "6.5 percent ...standard is used to exclude from the fluid milk product definition those products which contain some milk solids but which are not closely identified with the dairy industry, such as chocolate flavored drinks in "pop" bottles." Id.

There is No Justification for Changes to the Classification System.

The 6.5 percent exception has not been changed since it was established in 1974, and we believe that neither the petitioners nor AMS has presented sufficient evidence to warrant any changes at this time. In fact, AMS decided against

changing the 6.5 percent nonfat milk solids exception during Federal Milk Marketing Order (FMMO) reform that was concluded in 1998-99.

At that time, AMS noted that modifying or eliminating the standard would “greatly expand the fluid milk market category to include many essentially non-milk products that contain very little milk in them.” 63 Fed. Reg. 4802, 4924. (January 30, 1998) AMS also commented on how such a change could skew competition in the market by giving a competitive advantage to products that do not use dairy products and could lead to less use of dairy products as manufacturers reformulate their recipes to use little or no fluid milk in their products. *Id.*

These factors continue to hold true today. Any modification to the terms or the application of the 6.5 percent nonfat milk solids standard would, in AMS’s own words, “greatly expand the fluid milk market category to include many essentially non-milk products that contain very little milk in them.”

In general, agencies bear a heavy burden to justify changes to longstanding regulatory provisions. Given such a recent re-consideration of this provision, any effort to modify the current standard must be supported by compelling evidence, evidence which we submit has not been generated by petitioners or AMS. AMS should therefore refrain from making any changes to the current classification scheme.

Certainly, a wide array of new drinkable products in which milk is an ingredient continue to be developed by food and beverage manufacturers, and these products have been and continue to be appropriately classified under the current definition. The fact that some of these new products may fall outside of the Class I definition does not mean that the current definition needs to be changed.

These New Beverage Products Do Not Compete Against With or Substitute For Fluid Milk And Changing the Fluid Milk Definition May Reduce Usage of Milk as an Ingredient.

As I noted, the fundamental goal of the fluid milk definition is to cover products that compete with fluid milk. We do not believe there is any evidence demonstrating that these new products that contain milk as an ingredient are competing with or substituting for fluid milk.

Rather, we believe that these products are competing against soft drinks, juices, and bottled water, not fluid milk. There is simply no factual basis upon which to

conclude that any of the products that our member companies produce are competing with fluid milk for the same consumers. The decline in fluid milk consumption started long before our member companies began developing new products that utilize dairy as an ingredient. In fact, producers should applaud these new products, not try to penalize them by including them in the fluid milk product definition.

By increasing the cost of the dairy ingredients, reducing or eliminating the 6.5 percent standard, or the application thereof, could stifle innovation and could slow or even halt the development and introduction of new products. Products that are currently profitable may become unprofitable, while products that are marginally unprofitable but hold promise may simply be dropped. This would not only hurt companies and consumers, but it would also hurt producers by driving companies away from the use of milk as an ingredient in their products, leading to lower producer income.

Conclusion

In conclusion, the American Beverage Association believes that there is no basis to justify changing the current fluid milk product definition. Producers should be embracing the development of these new products that utilize milk or milk-components, which are helping to expand the demand for milk, and increase dairy producer income. Any effort to narrow the scope or application of the 6.5 percent exception or expand the Class I definition will result in companies seeking alternative ingredients wherever possible.

If AMS believes some action is necessary, then instead of making changes to the current regime, AMS should first conduct a thorough economic analysis to determine which products, if any, are competing with or substituting for fluid milk, and it should provide the opportunity for public comment on such analysis, before it moves forward with any recommended decision to modify the current fluid milk product definition. We are confident that such an analysis would demonstrate that our member's products are not competing with fluid milk, that our members help to expand the demand for dairy, thereby helping dairy producers, and that modifying the terms or application of the current fluid milk product definition would lead manufacturers to use other non-dairy ingredients in their products.

We appreciate the opportunity to comment on this matter, and we thank you for your consideration.